The Henry Fund
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NextEra Energy, Inc. (NEE)

November 12, 2021

Utilities

Stock Rating **HOLD**

Investment Thesis

NextEra Energy is a steady performer with ambitious growth plans, especially in the renewable energy space. Our DCF and EP models produce a price of $109 for a 27% upside, while our DDM yields slightly higher at $113 for a 31% upside. We are bullish on NEE's prospects through a recovering economy and spending plans that will benefit its products and services.

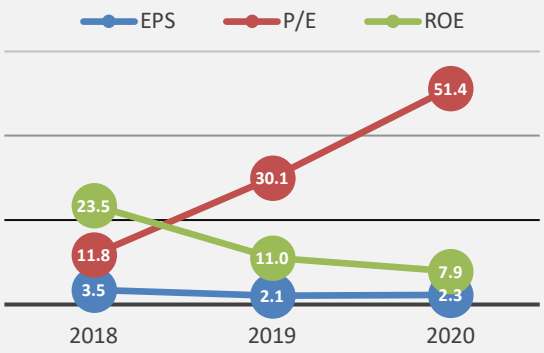
Drivers of Thesis

- Rising prices are a double edged sword for NEE. On the positive side, rate increases will boost revenue and could help improve the bottom line. See below for the risks that higher prices bring.
- NEE has seen steady margins through the first few quarters of the recovery from the pandemic downturn. It is on pace to see a slight uptick in net profitability and has maintained a strong credit rating through the challenges of the pandemic. These will keep the company in a good position to realize their growth goals.
- Capital expenditures in renewable projects will continue to increase operational efficiency and build NEE world-leading renewable generation portfolio. These technologies will be favored in the years to come as state regulators require higher renewable energy standards and infrastructure spending boosts these types of projects.

Risks to Thesis

- On the downside of rising prices, inflation could cause interest rates to climb steeply, which would raise borrow costs and hamper NEE's ambitious capital projects.
- Revenue growth for the industry has been sluggish of late. Should regulators not allow rate increases to offset rising input costs, margins could be hurt.

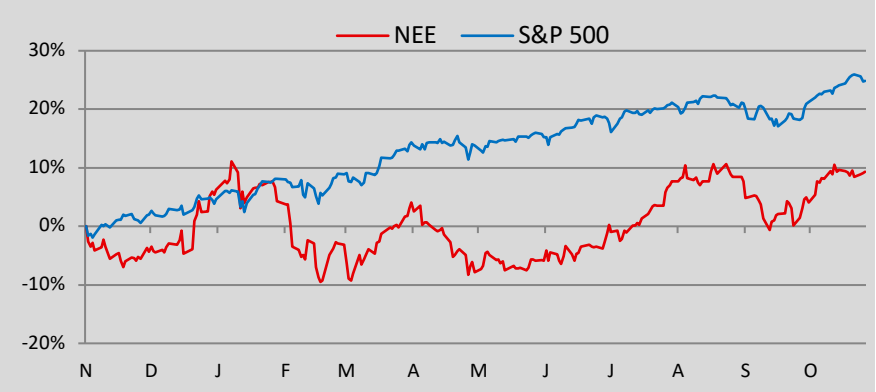
Target Price	$109-113
Henry Fund DCF-EP	$109
Henry Fund DDM	$113
Relative Multiple	$48
Price Data	
Current Price	$86.31
52wk Range	$68.33 – 87.69
Consensus 1yr Target	$91.30
Key Statistics	
Market Cap (B)	$167.5
Shares Outstanding (M)	1960
Institutional Ownership	78.5%
Beta	0.49
Dividend Yield	1.62%
Est. 5yr Growth	10.9%
Price/Earnings (TTM)	65.4
Price/Earnings (FY1)	36.8
Price/Sales (TTM)	9.4
Price/Book (mrq)	3.5
Profitability	
Operating Margin	28.4%
Profit Margin	16.2%
Return on Assets (TTM)	1.8%
Return on Equity (TTM)	5.2%



Earnings Estimates

Year	2018	2019	2020	2021E	2022E	2023E
EPS	$3.47	$2.09	$2.31	$2.40	$2.55	$2.77
HF est.				$2.35	$2.59	$2.83
growth	*21.86%*	*-39.77%*	*10.53%*	*1.73%*	*10.21%*	*9.27%*

12 Month Performance



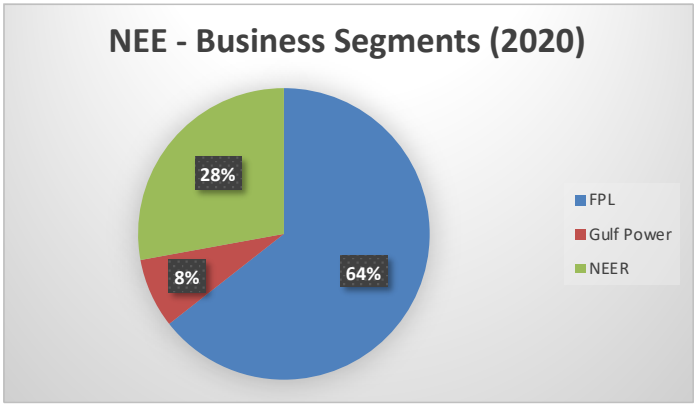
Company Description

NextEra Energy (NEE) is one of the major electric power companies in North America, employing just over 14,000 workers providing products and services across the entire value chain of the industry. It operates the largest portfolio of solar and wind energy generation through its subsidiary NextEra Energy Resources (NEER) and operates Florida Power & Light (FPL), an electric utility company that services major counties and municipalities throughout the Florida peninsula.

COMPANY DESCRIPTION

NextEra Energy (NEE) is one of the major electric power companies in North America, employing just over 14,000 workers providing products and services across the entire value chain in the utilities industry. Based on 2016 capacity, it operates the largest portfolio of solar and wind energy generation through its subsidiary NextEra Energy Resources (NEER). In addition to NEER, NEE operates Florida Power & Light (FPL), an electric utility company that services major counties and municipalities throughout the Florida peninsula. In 2018, FPL began the process of merging with Gulf Power, which added jurisdictions in 8 counties in the Florida panhandle. This public utility will continue to operate under the FPL moniker. According to the company's 2019 annual report, it operates 46,900 megawatts of generating capacity located in 30 states, four Canadian provinces, and Spain, although since the time of that report NextEra has exited its Spanish subsidiary and no longer operates in Spain.

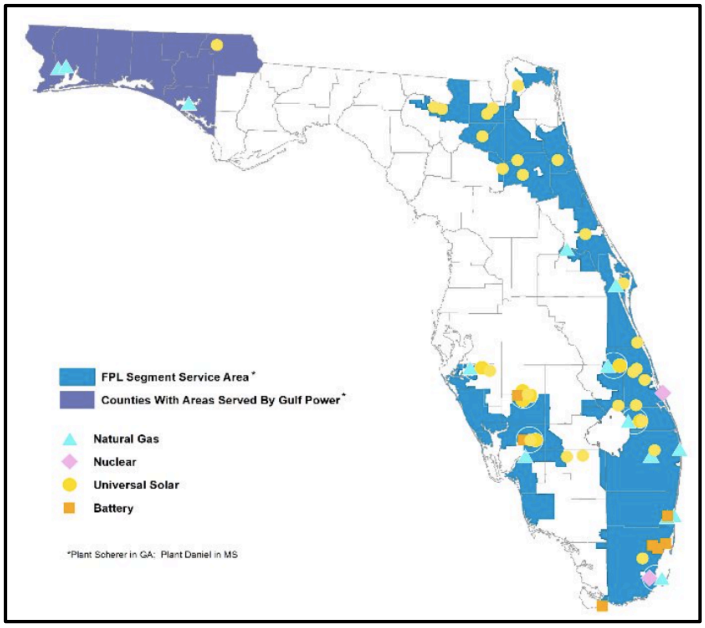
NEE controls 3.2% of the utilities market and in the five years leading up to 2021 has had an annualized growth rate of 5.1%, which leads over other major competitors Exelon (0.5%) and Duke Energy (2.8%).[1] This was largely supported by tax credits and favorable policies around green energy technologies, which NEE has invested in heavily. For 2020, NEE's segmented revenue breaks down to 64%, 28%, and 8% respectively for FPL, NEER, and Gulf Power[2], seen in the chart below:



Source: 2020 NEE 10-K Report

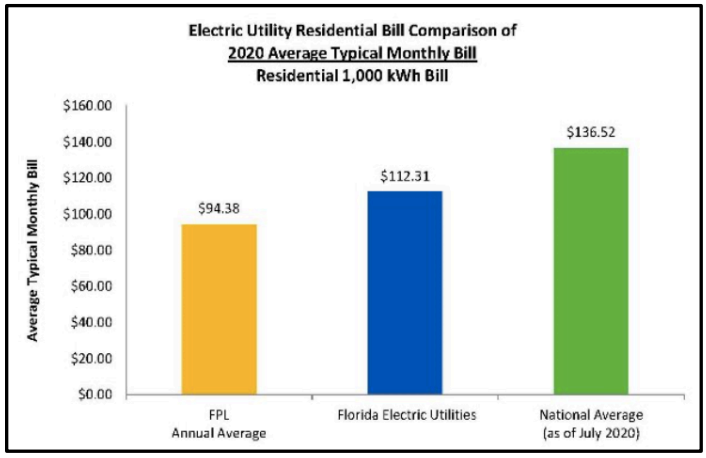
Florida Power & Light (FPL)

FPL is a rate-regulated public utility company that generates, transmits, distributes, and sells electric energy in Florida. It is the largest electric utility in the state and one of the largest in the country. As of December 30, 2020, had approximately 28,400 MW of generating capacity, 76,200 circuit miles of transmission and distribution lines, and nearly 700 substations. At the beginning of this year, FPL officially merged with Gulf Power, although they will still be regulated as two separate ratemaking entities until Florida regulators approve the consolidation of the two entities rates and tariffs. The combined companies now service more than 11 million people through more than 5.6 million customer accounts. FPL's operating revenues consist of residential, commercial, wholesale, and other customers, representing 58%, 32%, 3%, and 7% respectively. Their residential and commercial customers make up 89% and 11% of their total accounts, with industrial, wholesale, and other accounts at less than 1%.



Source: 2020 NEE 10-K Report

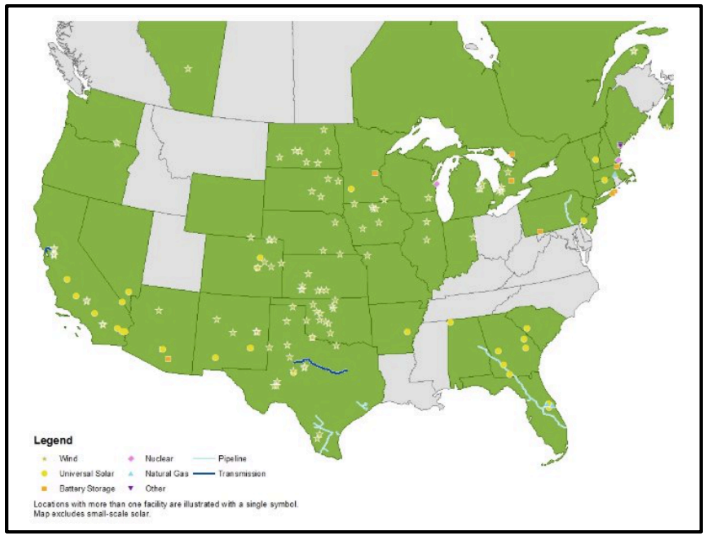
The price of 1,000 kWh of consumption per month is a standard industry benchmark for public utility companies. For 2020, FPL beat both the Florida and national average with their own average of $94.38 per 1,000 kWh of consumption per month, compared to $112.31 and $136.52 for the state and country respectively. Net generating capacity and net generation for 2020 came from four fuel types: natural gas, nuclear, solar, and coal. Capacity for each (as a percent of the whole) was 78%, 12%, 8%, and 2% respectively, while generation came in slightly different at 73%, 22%, 3%, and 2%. Over the historic period, FPL's share of NEE's total revenue hovered at or just below 70%, with the addition of Gulf Power bumping it up to 72.6% for 2020.[2]



Source: 2020 NEE 10-K Report

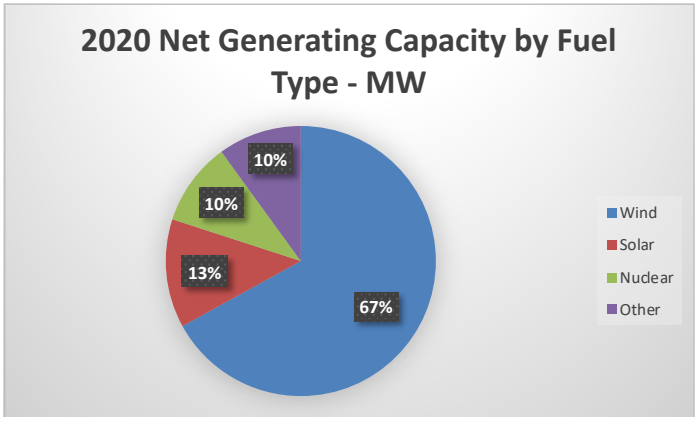
NextEra Energy Resources (NEER) & NextEra Energy Transmission (NEET)

NEER is NEE's diversified clean energy business with a strategy emphasizing the development, construction, and operation of long-term contracted assets with a focus on renewable projects. It operates in 38 states and 4 Canadian provinces, with an approximate total net generating capacity of 23,900 MW as of December 31, 2020. Wind power makes up two-thirds of NEER's capacity portfolio, with solar power at 13% and nuclear and other each at 10% (other consists mostly of natural gas assets). NEER also develops and constructs battery storage projects in effort to augment its renewable resources to better meet customer needs. Based on 2020 megawatt hours produced on a net generation basis, NEER is the world's largest generator of renewable energy from wind and solar.



Source: 2020 NEE 10-K Report

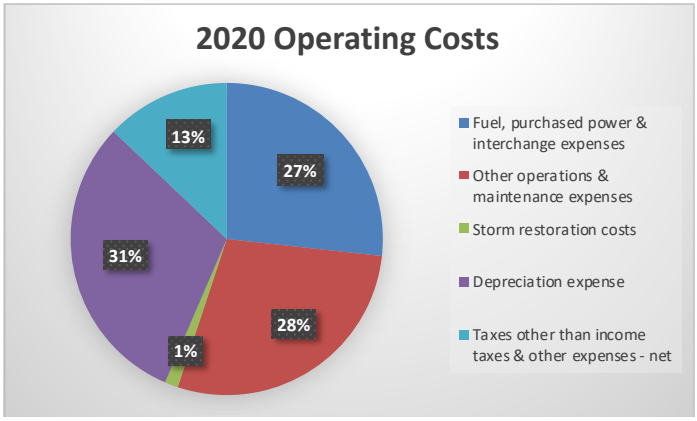
NEET is NEE's rate-regulated transmission business. It operates transmission facilities, primarily in Texas and California, with approximately 215 substations and 1,910 circuit miles of transmission lines. For financial reporting purposes, NEET is combined with NEER. Together, they represented 27% to 31% of NEE's total revenue over the historical period, with 2020 just at 28%.[2]



Source: 2020 NEE 10-K Report

Cost Structure

Fuel, operation & maintenance (O&M), and depreciation represent the bulk of NEE's costs, representing 26.7%, 28.3%, and 30.4% respectively for 2020. Over the historic period, operating costs ranged from as high as 79% to as low as 69%, with 2020 being right in the middle at 74%. Due to low fuel costs for the year, FPL's *Fuel, purchased power and interchange expenses* decreased by $640 million, where NEE's, because it is not using as much fossil fuel to begin with, only dropped $88 million. As a whole, operating revenue dropped 4.45% year-over-year from 2019 to 2020, but that was less than the decrease in revenue, so total operating expenses increased by 3.5%.[2]



Source: 2020 NEE 10-K Report

ESG Analysis

With a score of 26.9 at a medium risk level, NEE ranks 137th out of 606 utilities companies in the Sustainalytics ESG risk rating system. Sustainalytics also rates NEE with a *Medium* level of exposure to material ESG issues and a *Strong* level of response from the management of those ESG risks. Compared to its peers, NEE lands in the middle of the road, with Exelon and Avangrid scoring slightly better, and Duke, Sempra, and AES Corporation scoring 28.5, 30.2, and 35 respectively—the latter two scoring into the *High* risk category. Each company has a *Strong* rating for management response, and only NEE has a *Medium* rating for exposure risk, with all the others in the *High* group. It is unclear why they are ranked lower, perhaps because they have already invested heavily in renewable energy that might bring their exposure down.[3]

Sustainalytics ESG ratings:	Score	Rank
NEE	26.9	137
Exelon	24.4	106
Duke	28.5	162
Sempra	30.2	192
The AES Corp.	35	273
Avangrid	26.6	132

Source: sustainalytics.com

RECENT DEVELOPMENTS

Earnings Announcement – October 20, 2021

For third-quarter 2021, NEE reported adjusted earnings of $1,483 million for an EPS of $0.75, which compares to $1,311 and $0.67 EPS for the third quarter of 2020. These earnings beat consensus by $0.04, marking NEE's seventh straight quarter of higher than expected earnings. The beat was not enough to change management's long-term financial expectations, which anticipate an EPS range between $2.40 and $2.54 for 2021. Continuing into 2022 and 2023, the company expected 6% to 8% growth, with EPS coming in between $2.55 and $2.75 for 2022 and $2.77 and $2.97 for 2023.

	2021	2022	2023
Management Guidance - Low	$2.40	$2.55	$2.77
Management Guidance - High	$2.54	$2.75	$2.97
HF Model Estimation	$2.35	$2.59	$2.83

Source: 2021 NEE Q3 Earnings Release

Also in the third quarter of this year, NEER set a record for new renewables and storage origination, adding approximately 2,160 megawatts to their backlog since the close of the second quarter. Wind, solar, and storage represented 57%, 24%, and 16% respectively or 1,240 megawatts, 515 megawatts, and 345 megawatts of capacity added to each.[4]

Rate Settlement with Intervenors

In August, FPL reached a settlement with the Florida Office of Public Counsel, the Florida Retail Federation, the Florida Industrial Power Users Group, and the Southern Alliance for Clean Energy that will phase in new rates starting in 2022. This agreement will support long-term investments in infrastructure, clean energy and innovative technology—one such investment being the largest solar buildout in the United States. It will also continue to keep residential bills well below the US average. The agreement was approved in October by state regulators and is effective through 2025.[4, 5]

COVID-19 Impact

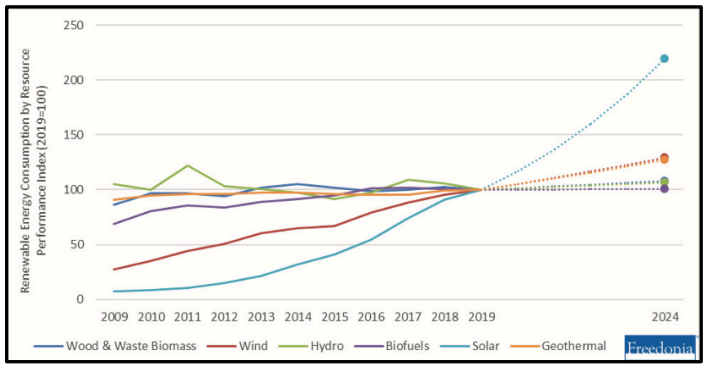
The coronavirus pandemic shifted the way electricity is consumed, away from commercial toward residential consumption. This is reflected in FPL's commercial and residential revenue breakdown for 2020. Their commercial segment dropped 12.6% year-over-year, representing not only the lowest drop in any given year of the historic period but also the lowest actual revenue of any year in the past decade. Meanwhile, residential revenue for 2020 was its highest of the decade, just barely edging out 2019. As such, the gains in residential did not offset the losses in commercial, so total revenue dipped by 4.35% for FPL year-over-year. This is largely explained by the pandemic. NEE does not consider this material to its operations, however, and expects to weather the pandemic well by continuing to implement processes and procedures to limit its impact on the business.[2]

Industry Trends

Renewables

Renewable energy consumption grew to a record high of 11.6 quadrillion Btu in 2020, representing 12% of US energy usage with its fifth straight year of growth. From 2009 to 2019, the industry saw an average annual growth of 3.9%. Production usually outpaces consumption to fulfill market demand. For 2019, production reached 11.8 quadrillion Btu and had a 4.1% average annual growth rate from 2009 to 2019. Total consumption and production of renewables is expected to reach 14 and 14.2 quadrillion Btu by 2024, respectively, for a 4.0% and 3.8% CAGR for

each. The largest gains are expected in wind and solar, with 5.3% and 17% estimated CAGR.[6]



Source: Freedonia Group – Renewable Energy: US

Removal of the Clean Power Plan (CPP) may slow renewable energy's exponential growth, but regional and local commitments to renewable energy may offset the loss of federal leadership. Regardless, wind and solar are not expected to surpass 20% of total electricity generating capacity by 2026. As of May 2021, 29 states had implemented Renewable Portfolio Standards (RPS), requiring utilities to increase their percentage of generation from renewables and thus increasing capital expenditures to build out that infrastructure. These costs were offset by subsidies and tax incentives.[1]

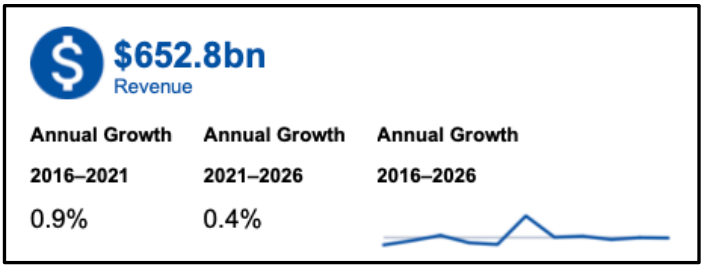
Two important tax credit incentives are the Renewable Electricity Production Tax Credit (PTC) and Solar Investment Tax Credit (ITC). Each credit operates a little different from the other, with the PTC offering a 1 cent/kWh produced credit toward federal corporate taxes and the ITC providing a credit of 22% of the installation cost of solar systems whose construction commenced in 2021. The PTC was recently phased down to 40% of its original starting amount of 2.5 cents/kWh in 2019 and will be completely phased out for any new capacity completed after the end of this year. Companies receive this incentive for the first ten years of the life of the generating asset. The ITC has also phased down from an original 30% credit in 2020 for systems coming online and 26% for systems whose construction commenced that year. It will continue to drop to 10% next year for systems commencing construction and will be 10% for any system stat does not begin service until 2023 regardless of the year construction started. NEE stated in 2019 that is does not see the phasing out of either of these credits as a threat to its operations.[7]

Regulations

This industry is regulated by the Federal Energy Regulatory Commission (FERC) at the federal level and public utilities commissions (PUCs) at the state level. Regulation is very high for this industry, as safety and environmental health are major concerns surrounding the industry's products and services. While the regulatory load is heavy on the industry, it also receives a lot of support from the government in the form of credits and other tax incentives. Prices and investment return levels are set by the government, which can limit the performance of the industry, but the governments involved are seeking safe, healthy, and stable utility systems, so successful performance is incentivized for all parties involved.[1]

Sluggish Revenue Growth, Yet Hopeful

Revenue growth over the previous five years has slowed due to a number of factors. These include declining population growth, household use of energy efficient technologies, stagnant manufacturing performance, electricity price growth that has not kept up with inflation, and natural gas prices that have declined. Positive performance in renewables have been a positive for the industry, but wind and solar, which are both expected to grow significantly over the forecast horizon, only account for a minor section of the industry revenue.



Source: IBIS*World* – Utilities in the US

Forecasted revenue growth will be driven by electric power generation and transmission growth that is expected to be higher than the previous five-year period. General growth in the broader economic will also help with demand, but the energy efficiency push will act as a headwind to this trend. In addition to electric power generation and transmission, natural gas is anticipated to grow, annualized at 0.5% over the coming 5-year period. Finally, continued recovery from the pandemic will help growth at the beginning of this period. Growth in natural gas will help that industry segment rebound from recent declines, and the retirement of tax incentives for

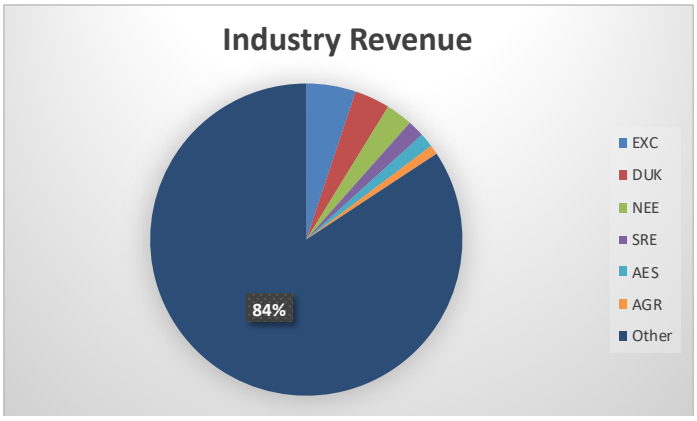
renewables and the Clean Power Plan (CPP) may slow coal's demise, at least in the short term.[1]

MARKETS AND COMPETITION

Companies operating in the utilities sector provide a variety of utility services, including electric power generation and transmission, natural gas distribution, steam supply, water supply, and sewage removal. These industries can be very different and even countervailing. Overall, the sector is dominated by electric power generation and transmission. Sector growth improved marginally over the five years leading to 2021, at an annualized rate of 0.9% to $652.8 billion. In the five years following 2021, that rate is expected to decrease to 0.4% to $664.5 billion by 2026. Renewables are still expected to make inroads in the market to the detriment of natural gas and coal, especially, but the price of natural gas will likely rebound after a sluggish time of late. The industry breaks down by products and services three ways: 1) electric power generation (18.6% revenue); electric power transmission and distribution (50.4%); and, other (31.0%). Sewage and water treatment accounts for a large part of the "other" category.[1]

Market Share and Comparison Financials

Companies in the utilities sector are typically major players in their respective regional and local markets. The top four companies account for only 12.5% of sector revenue, with the companies compared in this analysis comprising 16% of the market.[1]



Source: FactSet, IBIS*World* – Utilities in the US

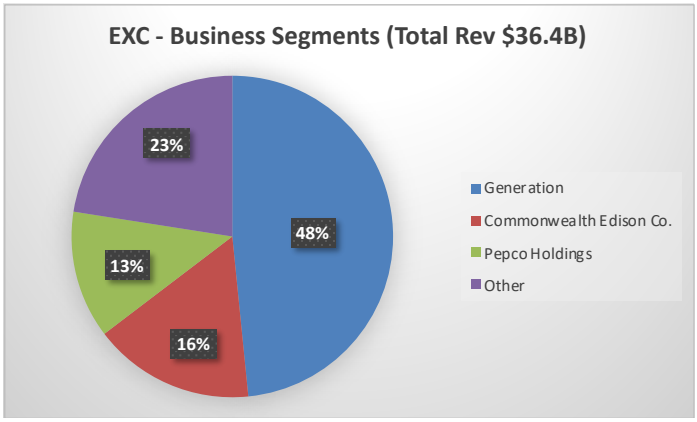
We compare NEE to five other utility companies with varying emphases in the sector: Exelon Corporation (EXC), Sempra (SRE), The AES Corporation (AES), Duke Energy Corporation (DUK), and Avangrid, Incorporated (AGR). The following table shows each company's performance in price-to-earnings ratio, EPS for the first three quarters of 2021, return on equity, operating margin, and market capitalization. NEE has by far the highest P/E ratio, nearly doubling Sempra, who is the next closest. Their market capitalization also dwarfs the next closest, Duke Energy, by more than doubling them. For the remainder, NEE has the second best performing operating margin, is third but well below the top two for EPS, and has half as good an ROE as the top performer.[8, 9]

	P/E	EPS	ROE	Op. Margin	Mrkt Cap (B)
NEE	65.4	$2.13	5.2%	15.2%	$167.5
EXC	28.3	$1.92	4.9%	6.8%	$53.5
SRE	33.8	$6.28	4.2%	7.5%	$38.8
AES	29.5	$1.09	10.0%	9.6%	$16.6
DUK	25.0	$4.29	6.0%	17.8%	$77.1
AGR	22.2	$1.83	N/A	13.4%	$19.6

Source: macrotrends.net, FactSet

Exelon Corporation – $54.40 (+31.0% YTD)

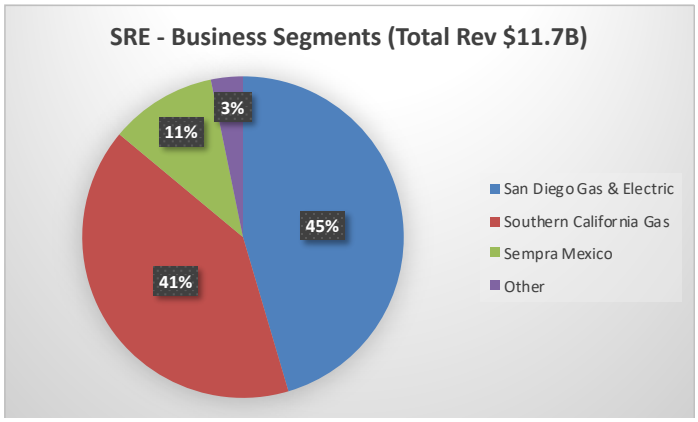
Exelon Corporation was founded in 1999. It is a Chicago-based company that primarily serves Maryland, Illinois, and Pennsylvania, who combined make up 66% of their customer base. In 2020, Exelon generated $33.0 billion in revenue, although sector-relevant revenue has declined annually 0.5% to $30.6 billion over the five years to 2021. They provide services across the whole value chain for the utilities sector, including generation, transmission, and distribution. Even though Exelon is the largest player in the sector, they only control 4.7% of the market, highlighting how low concentration is within the industry.[1, 10] EXC operates in four major segments: Generation, Commonwealth Edison Company, Pepco Holdings, and Other, decomposing as such for 2020:



Source: FactSet

Sempra – $122.10 (+4.2% YTD)

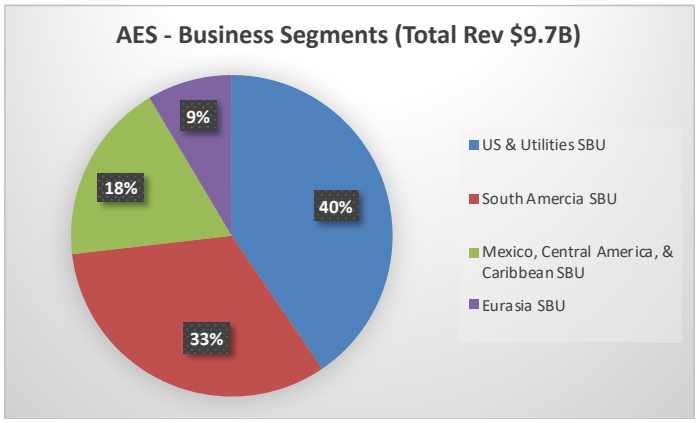
Sempra was founded in 1998 and is headquartered in San Diego, California. It owns and operates utility assets in California, Texas, and Mexico, with large holdings in primarily electricity and natural gas along the entire utilities value chain. It has a current market capitalization of $41.8 billion, with recent annual revenue hovering around $11 billion.[10] SRE operates in four major segments: San Diego Gas & Electric, Southern California Gas, Sempra Mexico, and Other, decomposing as such for 2020:



Source: FactSet

The AES Corporation – $24.72 (-2.8% YTD)

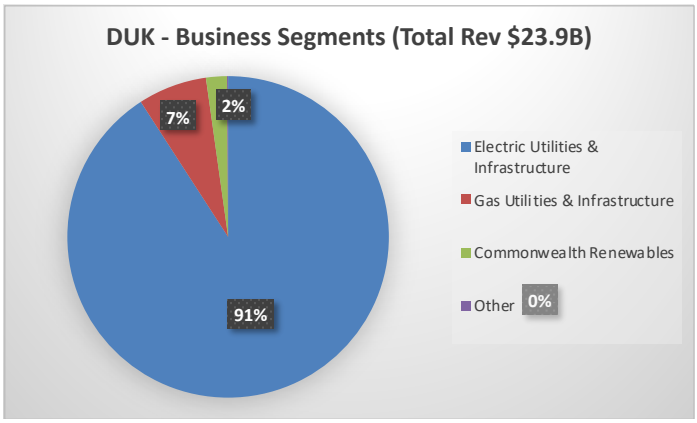
The AES Corporation operates a diverse portfolio of power generation assets and utility companies, services the Americas, Europe, and Asia. They generate power from the wide spectrum of sources, included many fossil fuel and renewable sources. The company was incorporated in Arlington, Virginia, in 1981 and has a current market capitalization of $16.6 billion and annual revenue around $10 billion.[10] AES operates in four major segments: US & Utilities Strategic Business Unit (SBU), South America SBU, Mexico, Central America & Caribbean SBU, and Eurasia SBU, decomposing as such for 2020:



Source: FactSet

Duke Energy Corp. – $99.88 (+11.1% YTD)

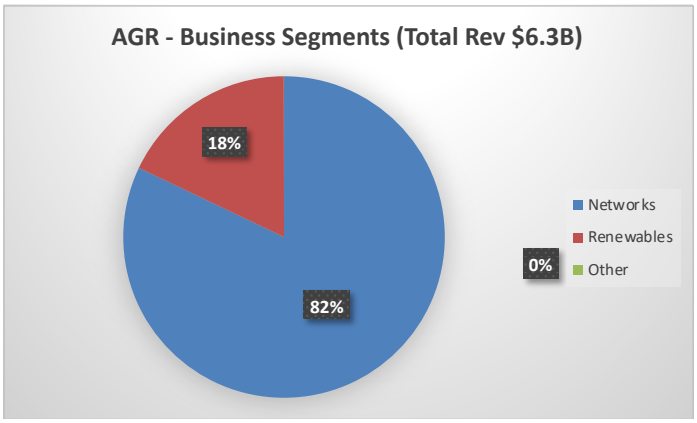
Duke Energy Company follows its roots back to the Catawba Power Company of the early 1900s. It is based in Charlotte, NC, and has a large workforce of nearly 30,000 employees in generation, transmission, and distribution across the Carolinas, the Midwest, Florida, Latin America and Saudi Arabia. They serve customers in these locales as well, providing products and services along the utilities industry value chain. Sector-relevant revenue grew at an annualized rate of 2.8% to $26.1 billion in the five years to 2021. Duke controls 4% of the utilities market.[1, 10] DUK operates in four major segments: Electric Utilities & Infrastructure, Gas Utilities & Infrastructure, Commonwealth Renewables, and Other, decomposing as such for 2020:



Source: FactSet

Avangrid, Inc. – $50.43 (+8.5% YTD)

Avangrid serves as an energy services holding company within two segments, renewables and networks. They also operate across a wide swath of both the electric and natural gas value chain, including generation, transmission, transportation, and distribution. They own eight electric and natural gas utilities in New York and New England, providing power to 3.3 million customers, and owns and operates 8.5 gW of electricity generating capacity through wind power in 22 states. Founded in 1852, they are headquartered in Orange, Connecticut, and are a subsidiary of Iberdrola, S.A. Their current market capitalization is $19.7 billion, with annual revenues just over $6 billion.[10] AGR operates in three major segments: Networks, Renewables, and Other, decomposing as such for 2020:

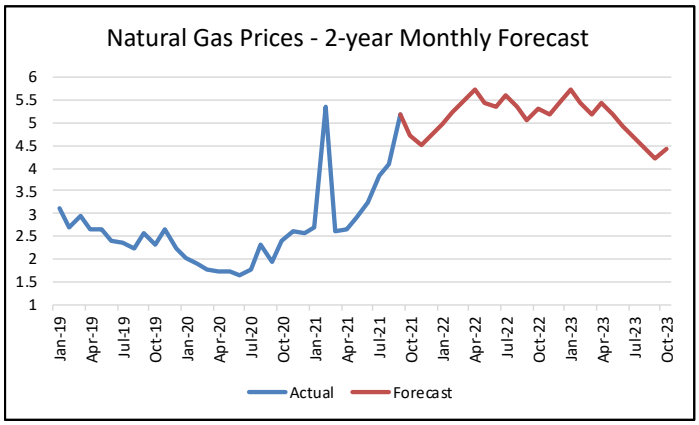


Source: FactSet

ECONOMIC OUTLOOK

Electric and Natural Gas Prices

Prices play a key role for utilities, especially the price of electricity and the price of natural gas. The price of electricity is expected to increase in 2021, which may curtail demand, but will be an opportunity for higher revenue for electric transmission utilities for the year. The price of natural gas, which is also expected to increase, can drive profits higher as the price increases, especially for utilities that generate electricity from natural gas, as opposed to just deliver natural gas to customers.[1]



Source: IBIS*World* – Utilities in the US

Historically, the price of electricity has been both input and demand sensitive. After the 2008 financial crisis, electric power prices fell mainly as a reduction in the input costs of natural gas and coal fell during that time but demand stayed relatively steady cause electricity is one of the last cost-saving measures of businesses in a crunch and one of the first to be used again after a downturn. Natural gas and coal prices steadily rebounded until a sharp downturn in 2014 and 2015, when renewable sources of electricity began to gain significant market penetration. Fortunately for electric producers, economic growth remained steady during this period, so the price of electricity was less effected than the price of natural gas and continued to see modest gains up to 2020.

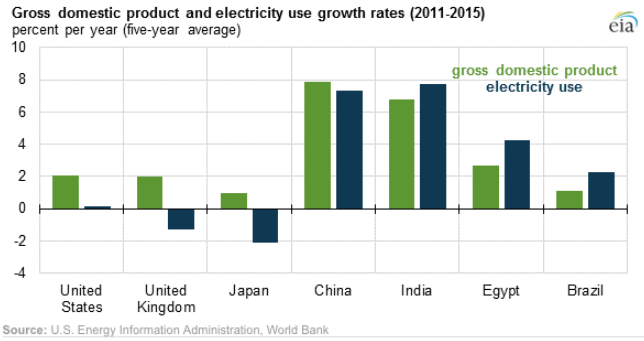
IBIS*World* forecasts the price of electricity to increase at an annualized rate of 0.9% over the five years to 2026, reaching 11.21 cents per kilowatt-hour. Demand for natural gas from developing countries and a growing domestic economy, as well as a possible return of demand for coal due to the higher LP prices,[11] will keep input costs high. Additionally, the Covid-19 pandemic has shifted electricity load away from commercial and industrial consumers and toward residential consumers. Though the long term effects of this remain to be seen, if the phenomenon persists, electricity prices will be more influenced by residential consumption habits. In the short term, IBIS*World* expects this to be more or less a wash, although slightly detrimental due to reduced overall demand. The economic recovery, however, is expected to mitigate reduced demand.[12, 13]

Electric Power Consumption

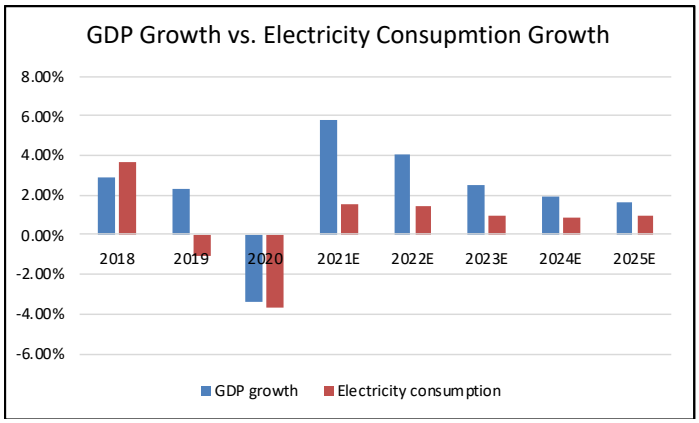
Pre-pandemic electric power consumption estimates were projected to increase by 0.6% per year, reaching 39.0 quadrillion Btu by 2024. The pandemic slowed this growth for 2020 and shifted some of the usage from commercial to residential, as well as reducing industry usage outright. Consumption, however, is expected to keep pace with economic growth as the world economy recovers from the pandemic recession. With a CAGR of -0.3%, electricity consumption was essentially flat in the five years leading up to 2019. Increased energy efficiency led to a decrease in per capita energy consumption, which when coupled with meager population and price growth led to sluggish revenue growth opportunities. Electricity generated from natural gas (30.6%), coal (28.6%), nuclear (22.7%), and renewables (17.4%) make up nearly all (99.3%) of the electricity consumed in the US for 2019. IBIS*World* has slightly higher growth prospects at 0.75% CAGR to the year 2027, but both growth rates are modest at best for consumption outlook in the near future. Like Freedonia, IBIS*World* highlights a recovering economy from the pandemic downturn, but they also see mitigation from manufacturing moving abroad and households continuing to seek energy efficiency.[14, 15]

GDP Growth and Electricity Consumption

Historically, GDP growth and electricity consumption have been linked, however, that link appears to break as countries become more developed. Increased electrification, shifting from a low-skilled manufacturing economy to higher-skilled manufacturing and a service-based economy, and relative income levels all play a role



in this phenomenon. For the first time in a decade, GDP contracted in the US in 2020, due to the economic cutbacks of the pandemic. Prior to this 3.4% drop, the five years leading up to the pandemic saw an average of 2.4% growth per year. GDP has bounced back in 2021, with growth expected to be just under six percent at 5.8%, the highest growth the US economy has seen since the mid-80s. The economy is projected to grow at an average of just over 2% for most of the remainder of our forecast horizon.[16, 17, 18]



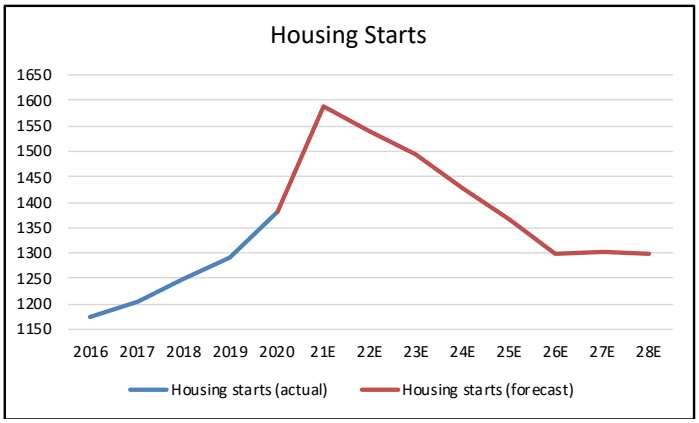
Source: IBIS*World* – US GDP, Electric power consumption

Electric Power Transmission

Overall, the outlook appears to be brighter in the coming five years than the previous five for electricity transmission business, with IBIS*World* projecting revenue to increase at an annualized rate of 1.1% to $434.7 billion in 2026 compared to a declining annualized rate of 0.8% for $411.4 billion in 2019. As mentioned above, reduced consumption played a big role in the decline over the past five years, but the improved consumption horizon, as well as the anticipated higher price for electricity, should help realize the anticipated gains.[19]

Housing Starts

With steady per capita disposable income, low new-home inventories, and a favorable borrowing environment in the years preceding the pandemic, housing starts saw modest growth in the five years leading to 2020, annualized at 3.2%. Though the pandemic might have been expected to reduce new housing starts, 2020 saw 6% growth over 2019 and 2021 is expected to see at least twice that with projections in the mid-teens. Five-year annualized growth after that is expected to decline at 3.2%, however, as borrowing conditions are expected to restrain demand. The overall outlook for the forecast period is positive and should help create heightened demand for electricity and boost industry revenue.[20]

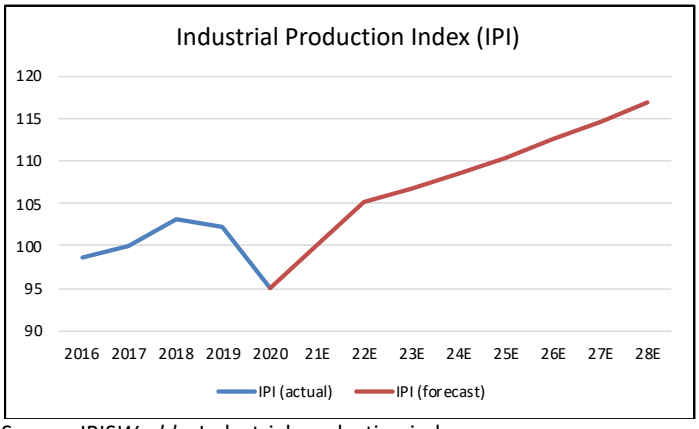


Source: IBIS*World* – Housing starts

Industrial Production Index

The industrial production index (IPI) measures output from varying sectors of the economy, including mining, manufacturing, and electric and gas industries. It is a performance metric driven by changes in productivity, credit access, and downstream demand in both domestic and international markets. The index is seen as a measure of total business activity and overall economic health. The IPI has had a clunky growth pattern over the historic period, ranging from a decline of 2.2% in 2016 to an increase of 3.2% in 2018, but has historically seen sustained growth after recessions, as seen after the dot com downturn (2002-07 all had positive growth) and the Great Recession (2010-14 saw increased). For this reason, analysts forecast the IPI to see sustained growth over the

next handful of years, with an annual growth rate of 2.1% from 2021 to 2025. This will be dependent on the broad economic recovery from the pandemic, however, but like new housing starts, if the index rises, demand for electricity should increase and revenues for the utilities sector will grow too.[21]



Source: IBIS*World* – Industrial production index

Inflation and Interest Rates

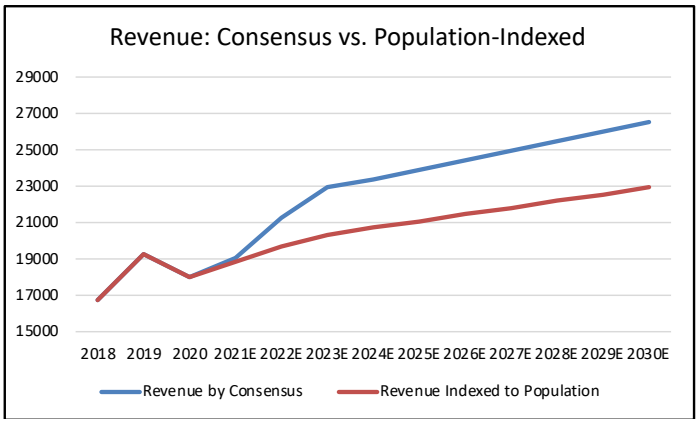
With the US seeing its highest inflation in 30 years, there are fears that the Federal Reserve may raise the federal funds rate, which would in turn raise borrowing costs. Prior to the pandemic, interest rates had been kept at historically low levels to boost economic growth after the Great Recession. Starting in 2016, the rate began to increase as the Federal Reserve sought to return to normal monetary policy. The pandemic, however, has brought the rate back down to inject liquidity into the economy, again lowering interest rates with a target rate of 0.10% early in the recovery and 0.25% today. If inflation continues to be a problem as the economy recovers, the Federal Reserve may need to choose between keeping rates low to massage growth and high inflation.[22]

VALUATION

Revenue Assumptions

NEE has two main forms of business, a regulated public utility that provides power for customers in Florida and an unregulated portfolio of assets that generate electricity sold on the open market. These are two different business models whose revenue streams should be considered separately, however, for the sake of the model, we decided to forecast NEE as a single unit but verify some of the assumptions using population statistics and projections. For the first three years of the forecast period, we follow consensus, then in the subsequent years we grow the revenue by the historic average.

Because the public utility portion of the business is subject to more regulation, it has tighter controls on how it is operated. Its revenue stream is closely linked to population growth, therefore it should be compared to historic and forecasted population growth trends. Over the historic period, the Florida population grew an average of 1.55% per year, from 19.1 million in 2011 to 21.9 million in 2020. Forecasted at this same clip, the population would grow to 25.6 million by 2030. Alternative projections provide a 2030 population range from 22.9 to 25.8 million, so the forecasted amount above hits these projection's higher range.[23, 24]



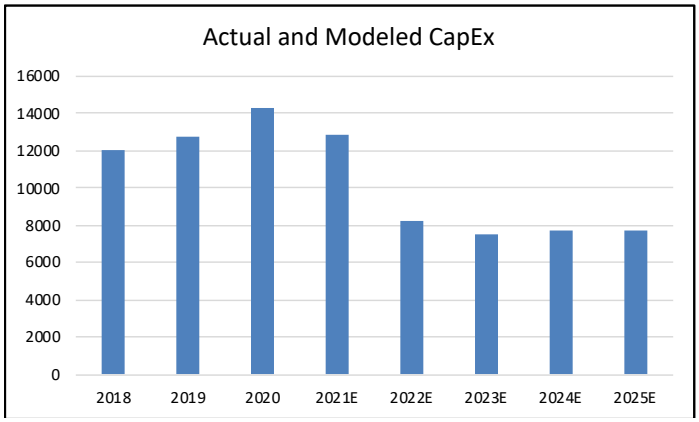
Source: HF Model, Bloomberg, FactSet

NEE has a low historic revenue growth rate, with years ranging from as high as 14.8% growth and as low as negative 7.6% growth for an average of 2.1% growth from 2011 to 2020. We assume consensus growth over the first three years of the forecast period, then grew revenue by the historic average. We compared this against a model that grew the unregulated business by consensus rates and the regulated business by the population growth. Through this analysis, we believe the consensus to be a bit aggressive, especially in the early forecast period, but the terminal values of each model are within reasonable proximity of each other to proceed with consensus.

Operating Cost and CapEx Assumptions

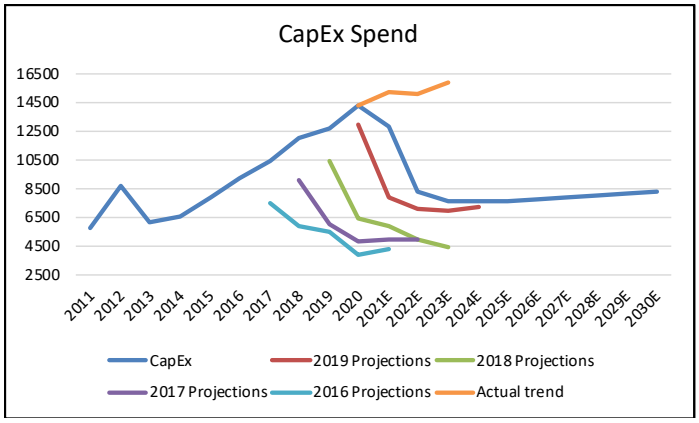
The most compelling story about the cost structure over the historic period is the reduction of *Fuel, purchased power & interchange expenses*, which constituted 52.3% of total operating expenses in 2011 and fell to 26.7% in 2020. This was largely driven down by the falling price of natural gas, which also fell 50% over the historic period. *Other operations & maintenance expenses* remained fairly

constant between 25.1% and 29.4% over the same timeframe, where depreciation and amortization expenses did the opposite of the fuel expenses by more than doubling from 13.1% to 30.6% of total operating expenses. This largely reflects NEE's accelerating capital expenditures, which grew from 37.4% to 79.7% of total revenue from 2011 to 2020.



Source: HF Model, 2020 NEE 10-K Report

For the fuel and other O&M costs, we kept the forecasted percentages consistent with their most recent percentages of total operating expenses, averaging 30.9% and 26.4% respectively over the forecast horizon. Fuel costs are expected to bounce back, so the slight jump from 26% to 30% is justified in that category. The capital expenditures are a little trickier to forecast, given not only their drastic movement over the historic period but also

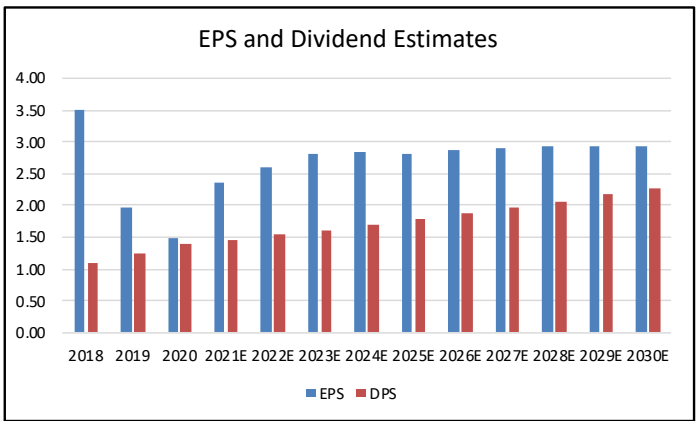


Source: 10-K Reports, HF Model

managements large projections over the first five years of the forecast period and their tendency in the past to overspend according to their forecasts (see graph above). The further out management forecasts, the more they overspend. We followed that guidance in our model for the first five years, then grew expenditures by an inflation rate of 2%. Regardless, we kept the depreciation and amortization expense between 16% and 17% over the forecast period. All this resulted in a stable cost structure over the forecast period, with total operating averaging 69.9% compared to its historic average of 74.2%.[2]

Margins and Profitability

With consistent cost structure, our margins are fairly consistent across the forecast horizon as well, with operating profit and net earnings averaging around 33% and 24% respectively. The averages for the forecast period are higher than the historic period but are not outside the range of the historic period for net profit, especially when reducing the historic period from ten to five years. Earnings per share are estimated to be $2.35, $2.59, and $2.83 for 2021, 2022, and 2023. This tracks toward the lower to middle range of management guidance.



Source: 2021 NEE Q3 Earnings Release

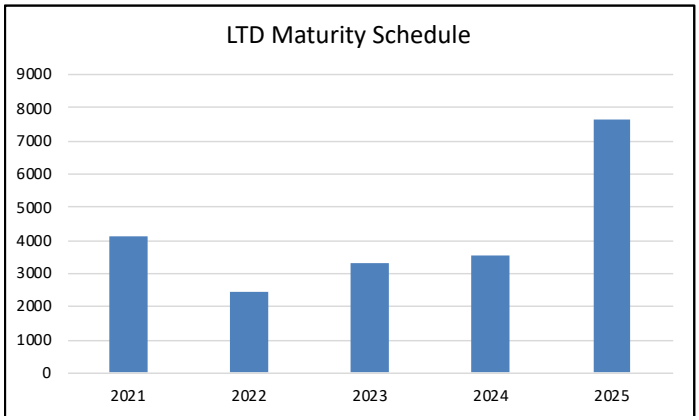
Capital Structure and WACC

Depending on the particular business entity holding the debt, NEE has investment grade debt ranging from BBB to A+ on the S&P rating scale, with exception of *NextEra Energy Oper Partners LP* who holds high yield debt with a BB rating. Overall, NEE debt position appears to be secure with little risk of default. For the purposes of our WACC formula, we averaged the yields on each of the entity's least mature bonds, calculating a pre-tax cost of debt at 3.13%. Here is how NEE's debt compares to its comps:

	S&P	Moody's	LTM/EBITDA
NEE	A+	Aa2	5.07x
EXC	A	A2	3.15x
SRE	BBB+	N/A	5.54x
AES	BBB-	N/A	5.05x
DUK	A	Aa3	6.14x
AGR	BBB	Baa1	2.83x

Source: FactSet, finra.com

NEE has an average debt to equity ratio of 1.3 over the historic period, but the trend has been downward over that time horizon, starting at 1.54 in 2011 but reaching 1.07 in 2020. The pandemic did not require NEE to increase its debt in a material manner, and we do not see that ratio changing substantially over the forecast period, so we have the ratio average 1.0 from 2021 to 2030. Our cost of equity and after-tax cost of debt are 3.46% and 2.46% respectively. We tried a handful of various averages for the beta but chose the five-year monthly, which came out to be 0.29. Put together, this gave us a weighted-average cost of capital of 3.2%.[25]



Source: 2020 NEE 10-K Report

Model Comparisons and Summary

Our discounted cash flow and economic profit models yield a price of $109 and our dividend discount model gives us $113, for respective upsides of 27% and 31% for each model. We are pleased that our models produce similar results, especially since NEE is a utility company that is expected to pay out regular, appreciating dividends. As such, our target price falls between these two models from $109 and $113, indicating NEE is currently undervalued and therefore recommending a buy. Ultimately, because we already hold the company above market weight, this translates to a hold.

With conservative revenue projections and favorable profitability margins over the forecast period, along with a cost of capital that reflects NEE's good credit rating and a rate environment that keeps cost low, we see a good argument to keep NEE in our portfolio. Our DCF, EP, and dividend discount models all provide a favorable upside that should continue to add value to the Henry Fund over the long term. Again, at $109 and $113 with 27% to 31% upside, we are recommending that we hold our current position in NextEra Energy.

KEYS TO MONITOR

The following are key indicators to follow to gauge NEE's performance over the next six to twelve months:

- **Economic Indicators**: NEE has a long list of economic indicators that could drive the performance of the stock. Close attention should be paid to all highlighted in this report, but perhaps of most note are prices, interest rates, and GDP growth, although the latter has proved less connected to electricity consumption in recent years. Higher input prices and retail and wholesale prices for electricity will drive both costs and revenue, but NEE's improving margins should help them take the most advantage of those higher prices. If inflation causes interest rates to rise sharply, NEE may have trouble raising the capital needed for big projects they have in the pipeline. This would dampen the stocks prospects.
- **Margins and Capital Expenditures**: Already hinted at, both margins and capital expenditures will be important measures of NEE's continued value. If NEE can carry through some of the gains in operating and profit margins it has seen at the beginning of the recovery, they will secure a stronger financial position that will help them fulfill more of their vision to remain the world leader in renewable energy.
- **Regulation and Infrastructure Investments**: Though not focused on greatly in this report, regulatory incentives to invest in renewables, as well as investments in green technologies with the infrastructure bill, could be good news for NEE. As the leader in solar and wind energy generation, they are positioned well to continue to expand their renewables portfolio and may catch a big windfall from new legislation aimed at addressing climate change.

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